



BUSINESS LAW SECTION

NONPROFIT & UNINCORPORATED ORGANIZATIONS COMMITTEE

THE STATE BAR OF CALIFORNIA

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April 6, 2009

Assemblymember Eng
California State Assembly
State Capitol, Room ??
Sacramento, CA 95814

Dear Assemblymember Eng:

I. Statement of Position

The Nonprofit & Unincorporated Organizations Committee (the “Committee”) of the Business Law Section of the State Bar of California (the “Section”) is pleased to sponsor Assembly Bill 404 (“AB 404” or the “bill”) and welcomes this opportunity to make comments in support of AB 404. This is the first statement of position that the Committee has submitted in support of this bill.

A. Description of AB 404

AB 404 requires the FTB to issue an acknowledgement letter when an organization requests tax exempt status under California law based upon the changes to Rev & Tax Code Section 23701d made by AB 897, which became effective January 1, 2008. Second, ABA 404 makes the acknowledgement letter or like document issued by the FTB a public document so the FTB may provide a copy of it to the public upon request. Third, AB 404 clarifies that an organization that is part of a federal group exemption may obtain tax exempt status under California law on the basis of the federal group exemption if the central organization and all of its subordinates are Internal Revenue Code Section 501(c)(3) organizations. Finally, AB 404 clarifies that if the FTB revokes an organization’s tax exempt status under California law, the organization may not reinstate its tax exempt status by merely submitting to the FTB its IRS determination letter.

B. HISTORY

Revenue and Taxation Code Section 23701d was added by Stats 1949, ch 557 § 1, effective July 1, 1951. As originally passed, it provided that an organization can apply to the FTB for a determination that the organization is exempt from tax. Assuming the FTB determines the organization qualifies as an exempt organization, the FTB issues a determination letter. Agencies and members of the public rely upon the determination letter to verify the organization's exempt status.

Section 23701d was amended by AB 897, effective January 1, 2008, to add a simplified procedure to obtain tax exemption under California law for an organization that already had received from the Internal Revenue Service a determination that it is a tax exempt organization under Internal Revenue Code Section 501(c)(3). Under the simplified process added by AB 897, a 501(c)(3) organization becomes tax exempt under California law upon its submission to the FTB of a copy of the determination letter from the IRS that states it is a 501(c)(3) organization.

C. The Problem

AB 404 greatly simplified the tax exemption process in California, but it also caused uncertainty and confusion in implementation. The purpose of AB 404 is to clarify the new simplified process for applying for tax exemption as a charitable organization under Revenue and Taxation Code Section 23701d.

D. The Solution

The Committee worked with the Franchise Tax Board to propose modifications to Sections 23701d and 19565 of the Revenues and Taxation Code, which modifications address four of the issues that arose from the passage of AB 897.

E. Committee's Position

The Committee recommends and fully supports AB 404 for the following reasons:

AB 404 requires the issuance of an acknowledgement letter by the FTB when an organization relies upon the simplified application procedure, , which was not required by AB 897 and is not required under current law. Other agencies rely upon a determination of tax exemption by the FTB, but the modification of Section 23701d by AB 897 did not allow the FTB to make a determination for those applying under the new simplified procedure; the discretion required to issue a determination letter was removed by AB 897 for organizations relying upon the new simplified procedure. That the FTB has not been able to issue a determination letter when an organization relies upon its federal determination letter to obtain state exemption has caused confusion. In the interim, the FTB has been issuing an "Exempt Acknowledgement

Letter” and issued FTB Notice 2008-3 that explained the purpose of the Exempt Acknowledgement Letter, but there is no statutory provision for such a letter. AB 404 codifies the mechanism for the FTB to issue an acknowledgement letter when the organization relies upon the simplified application for state tax-exemption (new FTB Form 3500A). AB 404 leaves in place the traditional method of applying for state tax-exemption (current FTB Form 3500) and obtaining a determination of the same from the Franchise Tax Board.

Although the FTB attempted to solve the problem created by the passage of AB 897 by the use of an “acknowledgement letter,” because the acknowledgment letter is not expressly a public document under current law, the FTB is unable to provide a copy of the letter upon request. AB 404 amends Section 19565 to provide that any documents submitted to the FTB to verify an organization’s exemption from taxation under 501(c)(3) of the IRC and the acknowledgement letter or other document issued by the FTB shall be open to public inspection. With this addition to Section 19565, the FTB will be able to provide copies of the same upon request and California agencies and members of the public will be able to obtain proof of California exemption from tax directly from the FTB.

It is unclear whether organizations exempt under federal law under a group exemption can take advantage of the simplified procedure for obtaining state tax-exemption provided by AB 897. Because California law and federal law are not in strict conformity regarding all organizations that are recognized as exempt under federal law under a group exemption, AB 404 clarifies that an organization that is part of a federal group exemption can apply for state exemption on the basis of the federal group exemption if the central organization and all of its subordinates are Internal Revenue Code Section 501(c)(3) organizations. (The Committee plans to recommend legislation next year to expand the simplified application procedure to tax-exempt organizations recognized under other sections of the Internal Revenue Code, and will work with the Franchise Tax Board on that effort.)

Finally, it is unclear that if the FTB revokes an organization’s exempt status under California law if the organization could then rely upon the simplified application procedure to reinstate its exempt status by merely submitting to the FTB a copy of its determination letter from the IRS. AB 404 makes it clear that an organization whose exempt status is revoked by the FTB must apply for exempt status under the procedure that requires a determination by the FTB and cannot seek to be reinstated by simply submitting a copy of their IRS determination letter.

II. Germaneness

The Committee believes that its members have the special knowledge, training, experience and technical expertise to provide helpful comments on the bill and that the positions advocated herein are in the best interests of California nonprofit tax exempt organizations and those they serve.

III. Caveat

This letter is that only of the Committee. The positions expressed herein have not been adopted by the Section or its overall membership or by the State Bar's Board of Governors or its overall membership, and are not to be construed as representing the position of the State Bar of California. There are currently more than 8,800 members of the Section. Membership in the Section is voluntary and funding for its activities, including all legislative activities, is obtained entirely from voluntary sources.

Very truly yours,

Nonprofit & Unincorporated Organizations Committee

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